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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	**MM Docket No. 93-215**
	)	
Rate Regulation	)	

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

COMMENTS OF COMCAST CABLE COMMUNICATIONS, INC.

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SUMMARY

The Commission has adopted a benchmark scheme for rate regulation which denies some cable operators, including Comcast, a fair rate of return on their investment. Any alternate proposal that permits operators to justify above-benchmark rates must, consistent with the guidelines and policies of the 1992 Cable Act, permit operators to recover a fair rate of return on investment while reducing the administrative burdens on consumers, franchising authorities, the Commission, and cable operators.

Constitutional Prerequisites. The Commission must adopt a ratemaking methodology that permits cable operators to recover the value of all assets, tangible and intangible, in addition to the external costs covered under the Commission's price cap scheme. The method must be constitutionally valid, and must protect the interests of both consumers and investors, as mandated by longstanding Supreme Court precedent. Due consideration must be given to factors unique to the cable industry; the Commission therefore may not simply adopt regulations based solely upon the regulation of telephone companies, for example. Essentially, the Commission must recognize that the cable industry is not a traditional utility and must therefore not be regulated as such. Harsh side effects, including a reduction in the quality of cable service may result from such treatment. Due consideration must be given to those factors unique to the cable industry, including the services provided.

Cable Differs From Traditional Utilities. The Commission must recognize that cable operators differ from utilities such as water, gas and electric, because cable

operators provide an almost infinitely variable product. Cable operators must consider hundreds of factors in evaluating the audience they serve and the type of programming they should offer. To attract a large subscriber base and retain the business of existing subscribers, operators must ensure that they provide high quality programming; and operators usually pay substantial premiums to acquire and retain such programming.

Rate of Return Regulation is Inappropriate. Unfortunately, the Commission's proposed cost-of-service methodology falls short of these standards and suffers from several flaws. As the Commission has recognized in the past, rate-of-return regulation is replete with shortcomings: increased administrative burdens, failure to replicate a competitive environment, failure in other regulatory contexts, and a faulty incentive structure, and the Commission has therefore rejected such a scheme. The proposed methodology suffers from the same imperfections. In particular, because the proposal fails to recognize the differences between the cable industry and traditional utilities, it fails to balance adequately consumer and investor interests. If the Commission were to adopt its proposal in whole or part, several classes of cable system owners would be grievously harmed financially. In particular, the proposed methodology would harm investors who have purchased systems at a price above book value with the expectation that their investment in tangible and intangible assets would be recovered over time. Many investors purchased cable systems in an unregulated environment in which actual book value was only a fraction of the value of systems. Investors expected to obtain a return on their investment over time in an unregulated environment. With regulation, the Commission has frustrated investor expectations, and must therefore offer a methodology whereby investors can recoup the above-book value of their acquired systems to be made whole.

Transition Mechanisms Are Required. A transition period has been used by the Commission and other regulatory authorities in the past to phase-in new regulatory programs. Such a transition must be integral to the Commission's ratemaking methodology adopted in this proceeding. The adverse impact on cable operators under a "flash-cut" approach would compromise the financial viability of cable systems that must justify initial rates. In any case, the methodology must not be administratively burdensome and should be streamlined.

The transition mechanism must incorporate a proper valuation method. A fair market valuation method is far superior to an original cost method. Alternatively, it may be feasible to value a cable operation based on its system or replacement cost if its fair market value cannot be accurately determined.

The Commission must recognize that the financial expectations and fiscal posture of most if not all cable operators determined the long-term rate structure adopted by the system owner. At the time of investment, the owner premised this rate structure on a long-term, unregulated environment. Thus, any regulatory system will frustrate an owner's long-term goals, and must therefore be developed to prevent such a result.

Comcast proposes in these comments a simple but effective system that permits recovery of intangible asset value through periodic adjustments to the rate, or Z factor adjustments, in addition to the permitted price cap adjustments. The Z factor is the value of an operator's net investment in tangible and intangible assets divided by the length of the recovery period. This mechanism is simple and fairly balances consumer and investor interests. Consumers are protected from major rate increases and investors can recover their entire investment.

Alternate Recommendations. Comcast is concerned that the Commission will adopt a single overall industry rate of return. The Commission is not compelled to adopt such a methodology — there are many other well-established cost-of-service methods that could be adopted. Several alternate methods may be used in lieu of an overall industry standard rate of return. For the initial showing, the target return should be the internal rate of return reasonably anticipated by an operator at the time of acquisition. Comcast also offers an alternate method to determine the cost of common capital as required under a conventional rate-of-return determination. Under this alternate method, the Commission could examine comparable groups to generate a recommended pre-tax overall cost of capital based on an analysis of comparable firms.

Even if the Commission decides not to adopt the proposal expounded in these comments, it must ensure that its alternate ratemaking methodology (1) permits cable operators to recover a fair return on investment, (2) properly balances the interests of consumers and investors, and (3) is not administratively burdensome.

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COMMENTS

Comcast Cable Communications, Inc., a subsidiary of Comcast Corporation ("Comcast"), by its attorneys, hereby submits its comments in the above-referenced proceeding. The Commission's initial order in the rate regulation docket adopted a benchmark scheme of regulation for cable television systems not subject to effective competition.[1/] In the instant proceeding, the Commission proposes alternate rules that will enable cable operators to justify rates above initially permitted rates.[2/] Specifically, the Commission proposes to adopt a ratebase valuation method, establish a rate of return, and adopt cost allocation and depreciation rules.

1/ Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Report and Order and Further Notice of Proposed Rulemaking, MM Dkt No. 92-266, FCC 93-177 (released May 3, 1993) ("Report and Order").

2/ Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Notice of Proposed Rulemaking, MM Dkt. 93-215, FCC 93-353 (released July 16, 1993) ("NPRM").

I. INTRODUCTION.

Given the fundamental changes that rate regulation will have on the cable industry and the limited time frame in which the new regulations must be formulated, Comcast believes that the Commission must initially focus on designing rules suitable for the justification of rates by systems newly subject to regulation and leave the task of long-term regulation for another day. These rules must take into account the financial and economic conditions of the cable industry and should allow operators to recover a company specific pre-tax overall rate of return on their total capital investment in a system. As an alternative, Comcast proposes a pre-tax overall rate of return based on an analysis of comparable firms.

Cable rates are a function of a number of factors, both internal and market driven. A rate methodology must identify all of those elements which are legitimate indicia of reasonable rates. For purposes of justifying existing cable service and equipment rates, the ratebase should contain the value of tangible and intangible assets, including the value of subscriber lists, the value of the franchise, and the going concern value. These elements represent the operator's investment in the system. As described herein, the exclusion of any of these factors from a newly regulated system ratebase would be inappropriate and legally suspect. On the other hand, their inclusion in the ratebase could serve to justify current rates and even, perhaps, rates in excess of current levels. In such cases, the operator may have chosen, for various reasons, to charge a lower rate expecting eventually to obtain a predicted return on investment.

Comcast is well aware of the importance of adopting a methodology that carefully considers consumer interests, without increasing rates unnecessarily. Rather than adopting a methodology that would trigger immediate rate increases, therefore, the Commission's rules should recognize the basis for higher rates but create a mechanism which postpones, but does not deprive, the operator's recovery of a reasonable return on its investment. In lieu of this higher rate, the operator should be able to charge the now justified rate and rates in the future that reflect not only permissible price cap increases[3/] but also amounts that will provide for recovery of and an adequate return on the net investment in the system over an established recovery period. This would be done by adding a Z factor to the annual increase allowed under price cap rules. The Z factor would reflect the value of intangibles (including a reasonable return on those intangibles), divided by the length of the recovery period. Current rates would remain frozen through April 4, 1994.

Finally, given that operators may have to justify their rates in response to complaints long before all the difficult questions raised in the NPRM can be

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3/ The Commission's price cap approach permits rate increases that reflect inflation and increases in taxes, franchise fees, costs of franchise requirements, retransmission consent fees, and programming costs. 47 C.F.R. § 76.922(d).

answered,[4] Comcast urges the Commission to defer consideration of particular accounting rules (e.g., rules governing depreciation, allocations, uniform systems of accounts, etc.) and other issues to a second phase of this proceeding.

II. THE COMMISSION MUST DEVELOP A RATEMAKING METHODOLOGY FOR THE CABLE INDUSTRY THAT IS CONSTITUTIONALLY VALID.

A. The Commission's Proposal Is One of Many Possible Approaches to Rate Regulation.

The NPRM proposes to adopt traditional telephone/utility-like rate regulation for cable operators. Typically, the rates a regulated enterprise may charge under this approach are adequate to cover its current expenses and allow a reasonable rate of return on investment. The NPRM proposes this "cost-plus" form of rate regulation "as the overarching standard to govern cost-based rates for cable service."[5] This method of utility-like regulation is not required by the 1992 Cable Act,[6] nor is it a methodology free of serious shortcomings, including the incentive it creates for

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4/ The Commission has extended to November 15, 1993, the time period for cable operators to respond to initial complaints concerning cable programming service, and to initial notices of regulation of the basic tier by local franchising authorities. Implementation of Sections of the Cable Television Consumer Protection and Competitive Act of 1992: Rate Regulation, Order, MM Dkt. 92-266, FCC 93-372 (released July 27, 1993). Nonetheless, the Commission will not have adopted new regulation in this proceeding until long after the November 15 deadline has passed.

5/ NPRM at ¶ 20.

6/ Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act").

regulatees to "goldplate" their facilities. It is odd that the Commission has recognized these shortcomings and has all but abandoned this regulatory methodology in other context,[7] yet suggests it be used to regulate the rates of cable operators.

The NPRM recognizes that the application of a traditional public utility cost-based rate methodology to the cable television industry is a major departure from pre-1984 regulation of the industry. In addition, the current financial practices and economic posture of heretofore unregulated cable operators differ substantially from those of companies that operate subject to cost-based regulation.[8] As a result, the Commission seeks comment on the impact of its proposed cost-of-service standards on cable operators and the need to establish a transition to enable cable operators to adapt to a rate-regulated environment.[9]

The NPRM proposes that a cable operator's regulated ratebase include plant in service, plant held for future use, and working capital. According to the NPRM, plant in service is likely to be the largest portion of the ratebase and it tentatively

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7/ Policy and Rules Concerning Rates for Dominant Carriers, Report and Order and Second Further Notice, 4 FCC Rcd 2873 (1989) ("Price Cap Order") and Erratum, 4 FCC Rcd 3379 (1989), modified on recon., 6 FCC Rcd 665 (1991) rev'd in part on other grounds, AT&T v. FCC, 974 F.2d 1351 (D.C. Cir. 1992); Second Report and Order, 5 FCC Rcd 6786 (1990) ("Second Price Cap Order") and Erratum, 5 FCC Rcd 7664 (1990), modified on recon., 6 FCC Rcd 2637 (1991), Nat'l Rural Telecom Assoc. v. FCC, 988 F.2d 174 (D.C. Cir. Mar. 26, 1993) (No. 91-1300).

8/ The Commission recognizes that its proposed regulations may "represent different measures of industry performance than currently used by the cable industry and lenders." NPRM at ¶ 22.

9/ Id.

concludes that traditional regulated utility "used and useful" and "prudent" investment standards applied to the original construction cost are the appropriate standards for valuing cable plant in service.[10/]

Although it identifies a number of methods used by regulators to determine the value of plant in service, the NPRM proposes to value cable system plant at original cost as a means to "produce lower rates for consumers while permitting cable operators to recover the costs incurred, by the current operator or the previous owner, in constructing assets used to provide cable television service."[11/] As discussed below, there are several critical flaws in this proposed ratebase valuation method as applied to the cable industry, particularly to systems that are no longer held by their builders. These comments demonstrate that there are other methods of rate regulation that are better suited to the diverse situations of cable operators and that are less onerous for the Commission to administer.[12/] In addition, it would be particularly

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10/ NPRM at ¶ 32.

11/ NPRM at ¶ 35.

12/ The Commission in the past has adopted alternate forms of regulation in lieu of rate-of-return regulation. The Commission has cited several shortcomings of the rate-of-return methodology. In its Price Cap Order, the Commission noted that its "experiences in travelling the second path of regulatory change in which we developed the existing rate of return structure, illuminate the difficulties of administering rate of return regulation under any circumstances." Price Cap Order, 4 FCC Rcd at 2889 (emphasis added). Among these difficulties are: (1) the burdens of administering the methodology, (2) its failure to duplicate competitive market results as intended, (3) the failure of the rate-of-return methodology in the past, and its inherent faulty incentive structure.

inappropriate to apply the proposed cost-plus methodology to previously unregulated business arrangements.

B. The Commission's Ratemaking Methodology Must Balance Investor and Consumer Interests.

At a minimum, the Commission must ensure that the end result of its rate order is constitutionally sound.[13] The Due Process Clause of the Fifth Amendment provides that the federal government cannot deprive a person of property without due process of law.[14] In the context of rate regulation, a due process violation occurs when the established rate is confiscatory, i.e., when it reflects an unjust and unreasonable balance of consumer and investor interests.[15] When considering investor interests, the Commission must ensure that the resulting rate is sufficient to allow the company to "operate successfully, to maintain its financial integrity, to

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13/ There is no statutory requirement that cable rates be governed by a rigorous cost-based methodology. Indeed, the specific language of the statute suggests that regulation was not intended to be as exacting as may be required for regulated utilities subject to Title II of the Communications Act of 1934, Pub. L. No. 73-416, 48 Stat. 1064 (1934). Although the Commission acknowledges the Congressional directive that cable regulation not mirror common carrier regulation (see, NPRM at 10 n.16), its proposal is very similar to that form of regulation.

14/ U.S. Const. amend. V.

15/ F.P.C. v. Hope Natural Gas, 320 U.S. 591, 602 (1944); see also, Washington Gas Light Co. v. Baker, 188 F.2d 11, 14 (D.C. Cir. 1950), cert. denied, 340 U.S. 952 (1951)("[T]here is a zone of reasonableness within which rates may properly fall. It is bounded at one end by the investor interest against confiscation and at the other by the consumer interest against exorbitant rates.").

attract capital, and to compensate its investors for the risks assumed . . . ."[16/] While the NPRM acknowledges that any rate regulation methodology must consider these interests, the net result of the Commission's proposal would deprive cable industry investors of a fair return on their investment, thus adversely affecting the industry's ability to attract capital. As Comcast explains in more detail herein, operators should justify their initial rates under a methodology that minimizes the immediate rate effects of system cost or purchase on subscribers. Such a methodology properly balances the interest of consumers and investors.

C. The Commission Must Give Due Consideration to Factors Unique to the Cable Industry When Developing Its Rate Methodology.

Whether the Commission's regulatory scheme will produce a rate that will allow a company to "operate successfully" and "compensate its investors" will depend on the circumstances under which such regulation is imposed.[17/] Simply because a particular regulatory methodology has been found constitutional does not mean that it will produce an appropriate or constitutional result in another context.[18/] In order to

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16/ Hope, 320 U.S. at 605. See also, City of Chicago v. F.P.C., 458 F.2d 731, 750 (D.C. Cir. 1971), cert. denied, 405 U.S. 1074 (1972).

17/ Hope, 320 U.S. at 605; See also, Farmer's Union Cen. Exch., Inc. v. ARCO Pipeline Co., 734 F.2d 1486, 1502 (D.C. Cir. 1984), cert. denied, 469 U.S. 1034 (1984). ("The delineation of the 'zone of reasonableness' in a particular case may, of course, involve a complex inquiry into a myriad of factors.").

18/ Jersey Cent. Power & Light Co. v. F.E.R.C., 810 F.2d 1168, 1180 (D.C. Cir. 1987) ("The fact that a particular ratemaking standard is generally permissible does not per se legitimate the end result of the rate orders it produces.").

be legitimate, therefore, the end result of the method's application must be legitimate as applied to the specific circumstances at hand in light of all relevant factors.[19/] Because of the significant differences between the cable industry and traditional utility companies (accounting and financial practices, capital structures, etc.), the Commission must take care to craft regulations appropriate to this industry. It cannot, for purposes of administrative convenience, simply impose on the cable industry a regulatory framework designed over the years for application to typical regulated utilities.[20/]

1. Cable is Not a Traditionally Regulated Utility.

Cable operators are not traditional utilities or common carriers that have been subject to original cost regulation for decades.[21/] When investments are made in a traditional utility, investors are aware that the return on their investment is directly

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19/ Bluefield Waterworks & Improvement Co. v. Public Service Comm'n, 262 U.S. 679, 692 (1923).

20/ "To regulate such an enterprise by undiscriminatingly transplanting any body of rate doctrine conceived and adapted to the ordinary utility business can serve the public interest . . . if at all, only by accident . . . . If . . . rates are intelligently to be regulated we must fit our legal principles to the economy of the industry and not try to fit the industry to our books." Hope, 320 U.S. at 649-50 (Jackson, J. dissenting).

21/ Congress did not intend that cable operators be regulated like common carriers. "The Committee is concerned that several of the terms used in this section are similar to those used in the regulation of telephone common carriers. It is not the Committee's intention to replicate Title II regulation." H.R. Rep. No. 628, 102d Cong., 2d Sess. 83 (1992) ("House Report") (emphasis added).

affected by regulatory policy. Investments made in an unregulated environment cannot reasonably be treated the same as those made in a regulated environment. Investors take into account the circumstances existing at the time investments are made.[22/] While there are inherent risks associated with any business venture, an investor should be able to rely reasonably on the fact that the government will not take away its ability to earn a return on past investments.[23/]

Congress and the Commission have "changed the rules" affecting the cable industry twice in ten years, first deregulating the industry pursuant to the 1984 Cable Act,[24/] then regulating it in 1992. Today's "reregulation" varies dramatically from the permitted scope and/or nature of earlier regulation.[25/] As pointed out by the

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22/ As the Court stated in Bluefield: "Investors take into account the result of past operations, especially in recent years, when determining the terms upon which they will invest in such an undertaking" 262 U.S. at 694.

23/ As discussed infra, the Commission has recognized this principle in other contexts by allowing telephone companies to fully amortize over the course of ten years the embedded, capitalized accounts of deregulated inside wire which appeared on their books. See Amendment of Part 31, 85 FCC 2d 818, 829 (1981).

24/ Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2780 (Oct. 30, 1984) ("1984 Cable Act").

25/ Although cable operators were subject to various forms of state and local regulation, the scope of permissible regulation was quite limited. Regulation of nonbasic cable service was completely preempted by the Commission. See, Community Cable TV, Inc., 95 FCC 2d 1204 (1983).

Supreme Court in Duquesne, there are special constitutional issues associated with such radical changes in policy:

> [A] decision to arbitrarily switch back and forth between methodologies in a way which required investors to bear the risk of bad investments at some times while denying them the benefit of good investments at others would raise serious constitutional questions.[26/]

Switching back and forth, not between methodologies but rather between regulation and nonregulation, creates the possibility that investors who purchased and improved systems prior to regulation will be denied the benefit of good investments. Even if an investor could have anticipated future regulation of the industry it could not have anticipated that new regulation would be so pervasive.

2. Regulatory Policy Must Consider Market Realities.

An active market has developed for cable systems and companies; transfers of ownership of cable companies have occurred regularly at prices controlled by market supply and demand. The presence of an active marketplace is a significant factor in determining the minimal legal requirements for regulation. The Supreme Court has found that setting rates based on the actual present value (the "fair value" rule) gives companies "strong incentive to manage their affairs well and to provide efficient service to the public . . . ."[27/] Nevertheless, the fair value standard was abandoned as a constitutional requirement because of "the laborious and baffling task of finding

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26/ Duquesne Light Co. v. Barasch, 488 U.S. 288, 315 (1989).

27/ Id. at 309.

the present value of the utility . . . [whose] assets were rarely bought and sold."[28/]
This limitation does not apply to the cable industry.

3. Cable Television is Not An Essential Service Like Water or Electricity.

The Commission's rate methodology also must consider present and future risks of the cable television industry. The Supreme Court commented that "[t]he risks a utility faces are in large part defined by the rate methodology because utilities are virtually always public monopolies dealing in an essential service, and so relatively immune to the usual market risks."[29/] The same cannot be said about cable systems. A traditional utility (e.g., telephone, gas, electric, etc.) has a state-granted monopoly for an essential service.[30/] This guarantees nearly 100 percent penetration of its market.

Although a cable company may have a government-granted non-exclusive franchise, the franchise is neither protection against competition nor a guarantee that

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28/ Id. at 309 n.5 (citations omitted).

29/ Id. at 315. See also, Willcox v. Consolidated Gas, 212 U.S. 19, 51 (1909) ("The complainant [Consolidated Gas Company of New York] has a monopoly in fact, and a consumer must take gas from it or go without. He will resort to the 'old stand,' because he cannot get gas anywhere else."); Los Angeles Gas & Elec. Corp. v. Railroad Comm'n, 289 U.S. 287, 300 (1933) (where gas utility had a history of successful business, no real competition and the probability of continued demand was assured, the "hazard" faced by the company was small).

30/ Although some states have begun to reduce entry barriers for potential alternative providers of telephone services, competition in local switched telephone service is virtually non-existent.

nearly 100 percent of potential customers will purchase its product. Cable operators face competition in various forms, including other multichannel video distribution services, over-the-air channels and other entertainment sources. Moreover, unlike water or electricity, cable television is a discretionary service that many households elect not to purchase.[31/] As a rule, even the most successful of cable television systems is not immune from "usual market risks."[32/]

Decade upon decade of utility regulation has been built upon a foundation of "limited risk" for the regulated party. The Commission must recognize, however, that this paradigm has little relevance for the post-1992 cable industry. Comcast respectfully submits that constructs appropriate for regulating the natural gas industry in 1944 will not serve to balance investor and consumer interests with respect to the cable industry in 1993 and beyond.

31/ Traditional utility services are considered necessities, hence from the day they begin service, they serve nearly 100 percent of the market available to them. This is not true for a cable television system which must develop its market. Three to four years of early losses is the norm for a new system. Even after several years a mature cable system may serve only 60 percent of this market. For example, Comcast systems in Flint, MI, West Palm Beach, FL and Orange County, CA have each been in operation for 15-20 years and have achieved penetration levels of 57 percent, 46 percent and 43 percent, respectively.

32/ Practical evidence of these differences is manifest in the financial market's perception of cable versus traditional utilities. While many utilities enjoy relatively high investment ratings, few cable companies have even achieved investment grade ratings.

4. Cable Television Represents a Variable Product That Will Suffer if the Commission Adopts an Inappropriate Ratebase Valuation Methodology.

In addition to operating under heightened risk levels, cable operators differ from providers of essential services like water, gas and electric, because cable operators provides an almost infinitely variable product. Unlike essential service providers, which must supply a consistent level and quality of service (generally mandated by regulation), cable operators typically make hundreds of decisions regarding the programming ultimately delivered to their subscribers. While "quality" of programming is obviously a subjective measure, cable operators continually exercise an important editorial function that affects the very nature of the product delivered to subscribers. Comcast submits that, under a confiscatory rate scheme such as that tentatively proposed by the Commission, a cable operator's fixed costs can be recouped in only one way: by reducing variable costs including those associated with program offerings. Reduced investment in programming could reduce the quality of products provided on the system. Not only is this counter-intuitive from a policy standpoint,[33/] constitutional issues appear to be implicated as well.[34/]

33/ For example, between the years 1986 (when cable rates were deregulated) and 1992, the number of basic cable subscribers in the United States grew from 42 million to over 57 million, an increase of 35%. During the same period, cable programming expenditures increased from $2 billion annually to $3.8 billion, a 90% increase. National Cable Television Association, Cable Television Developments (February 1993). Despite the fact that monthly cable bills also were increasing during this period, subscribers seem to have been willing to pay more for better product and greater variety. Therefore, any decision by the Commission that would decrease program quality would ultimately appear detrimental to consumer welfare.

A regulatory policy which has even an incidental effect on speech invites a different level of scrutiny. Regulations that undermine an operator's ability to deliver product of a particular intended nature or quality is a form of confiscation that does not arise in the context of traditional utility regulation. While regulatory agencies often have struggled to reconcile the traditionally adversarial interests of investors and consumers, investors and consumers will both be made better off if investors are allowed a reasonable return on their investment.

D. The Commission Should Not Consider Inappropriate Factors in Setting Cable Rates.

The factors that distinguish the cable industry from traditionally regulated utilities must be considered in determining the appropriate methodology for measuring rates. The Commission, however, has proposed to take into account one factor that is clearly not relevant — how particular rates compare to the Commission's benchmark rate levels.[35] Comcast submits that any such comparison is irrelevant for legal and ratemaking purposes.

The Commission has expressed its intention to have benchmarks and price caps comprise the "primary method of regulating cable service rates."[36] The

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34/ (...continued)
34/ Unlike regimes that regulate the cost of gas or water, the Commission's rules that establish the components of a cable operator's ratebase will have a direct impact on the content of the regulated party's speech.

35/ NPRM at ¶ 7.

36/ NPRM at 10 n.16; Report and Order at ¶ 262.

Commission envisions its cost-of-service proposal as a necessary "backstop" methodology for those instances in which the benchmark framework will not "permit cable operators to recover the reasonable costs of providing regulated cable service."[37/] The Commission recognizes that it "cannot be certain that the initial [benchmark or permitted rate] will permit all cable operators to fully recover the costs of providing basic tier service and to continue to attract capital."[38/]

At the same time, the Commission suggests that the cost-based rate methodology be designed to achieve rate levels "in relation to benchmark rates."[39/] It even suggests that an appropriate goal might be to produce rates "that approximate competitive rate levels, i.e., rates that approach the operators costs."[40/] Although such a goal may seem reasonable at first blush, it is totally inconsistent with the stated

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37/ Id. In an apparent effort to discourage operators from using its "backstop" methodology, the Commission has authorized local franchising authorities to impose a rate lower than the permitted benchmark for any system that elects to justify rates based on costs. Report and Order at ¶ 272. This "threat" is completely inconsistent with the Commission's stated regulatory theory.

If one accepts the premise that the Commission's benchmarks achieve their goal of generally providing appropriate levels of compensation for cable operators, then only cable systems facing special circumstances or abnormally high costs will elect to engage in the burdensome process to justify rates. Because a cost showing is a means by which individual operators can demonstrate the inadequacy of rates at benchmark levels, there is little likelihood that it would reveal that an operator's rate should be below its benchmark rate level, unless the cost methodology is itself seriously flawed.

38/ Report and Order at ¶ 262.

39/ NPRM at ¶ 7.

40/ NPRM at ¶ 10.

objectives of the Commission's "backstop" cost-based regulation. The Commission purportedly has identified those "competitive rate" levels through the benchmarks.[41/] It has also said that the benchmark permitted rates may be inadequate in some situations. It cannot, then, use the "backstop" methodology to achieve those same rate levels. The purpose of justifying rates is to enable operators in special circumstances to demonstrate why the Commission's competitive rate levels are not adequate.

III. BY FAILING TO RECOGNIZE THE DIFFERENCES BETWEEN CABLE OPERATORS AND TRADITIONAL UTILITIES, THE COMMISSION HAS FAILED TO BALANCE ADEQUATELY INVESTOR AND CONSUMER INTERESTS.

The Commission's proposal to adopt a ratebase regulation methodology that excludes large portions of a cable operator's investment overlooks the realities of cable system economics and therefore will result in rates that are confiscatory.[42/] First, the NPRM fails to recognize that cable operators have functioned in an unregulated environment in which plant in service is only a part, perhaps even not the most important part, of the value of a cable system. Although the Commission

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41/ Comcast submits that the Commission's benchmarks do not, in fact, reflect appropriate levels of compensation because, among other infirmities, the benchmarks fail to take into account the reasonable profit factor as required by the 1992 Cable Act and fail to account for the statutory distinctions assigned to basic and cable programming services. See, e.g., Booth American Co., et al. Petition for Reconsideration.

42/ See, Jersey Cent. Power & Light Co., 810 F.2d at 1189 (when an unreasonable balance is struck in favor of rate payer interests, the resulting rate is confiscatory).